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**DISCOVERY MINES
LIMITED**

1980

ANNUAL REPORT

DISCOVERY MINES LIMITED

DIRECTORS

J. C. BYRNE, Toronto
Chairman and Chief Executive Officer, Rayrock Resources Limited

E. G. CHRISTENSON, Oshawa, Ontario
Vice President, Finance, Rohm and Haas Canada Inc.

D. R. CROMBIE, Toronto
President and Operations Manager, Rayrock Resources Limited

E. E. CURRY, Calgary, Alberta
Chairman, Precambrian Shield Resources Limited

J. S. LIVERMORE, Reno, Nevada
Manager, Cordex Exploration Company

W. STEUERMAN, Toronto
Secretary-Treasurer, Rayrock Resources Limited

H. J. WHELAN, Toronto
President and Chief Executive Officer, Lummus Canada Inc.

OFFICERS

J. C. BYRNE
Chairman of the Board and Chief Executive Officer

D. R. CROMBIE
President and Operations Manager

W. STEUERMAN
Secretary-Treasurer

SENIOR GEOLOGIST

T. Antoniuk

EXECUTIVE OFFICE

Suite 1011, 2200 Yonge Street, Toronto, Canada

TRANSFER AGENTS AND REGISTRARS

CROWN TRUST COMPANY, Toronto.

BANKERS

ROYAL BANK OF CANADA, Bay and Temperance Branch, Toronto

AUDITORS

COOPERS & LYBRAND, Toronto

SOLICITORS

CAMPBELL, GODFREY & LEWTAS, Toronto

ANNUAL AND GENERAL MEETING

May 29, 1981, 10:00 a.m.
Alberta Room, Royal York Hotel
Toronto, Canada

DISCOVERY MINES LIMITED

Directors' Report to the Shareholders:

1980 HIGHLIGHTS

- Interest in two new gold producers
 - Exploration agreements on three gold properties
 - Working capital increased by \$1,806,000
 - Large increase in value of effectively controlled Rayrock Resources
-

MINING

Discovery's associated company, Rayrock Resources Limited, owns 26.5% and manages the 1,000 ton per day Pinson open pit gold mine in Nevada. The plant was constructed and the mine developed during 1980 at a total cost of US \$18,800,000 and production started on schedule in January 1981. By February, the mill recovery and grade of mill feed were right up to plan. Reserves at Pinson in the main pit are 3,250,000 tons grading 0.12 ounces gold per ton, plus approximately 5,000,000 tons of low grade heap leach material. Additional reserves within trucking distance of the mill are controlled by the Pinson group. The mine will produce a substantial cash flow for Rayrock.

The Gordon Lake, Northwest Territories, gold property, two-thirds owned by Discovery, was brought into production in July 1980, on schedule. Results to year end, however, have been below expectations, a result of power plant failures and problems in the mill and in the mine. Diamond drill results below the bottom 1,000 foot level indicate that the main vein continues strong with some excellent gold values as follows:

Hole No.	Intersection	Depth Below 1,000' Level
	Uncut	
U-80-1	1.626 ounces per ton across 12.9 feet	60 feet
U-80-2	2.648 ounces per ton across 21.2 feet	120 feet
U-80-3	0.345 ounces per ton across 12.0 feet	155 feet
U-80-4	Missed the Main Vein	275 feet

These intersections are in the wide, best grade portion of the Hump Vein.

The property is leased to Noranda Mines and Pamour Porcupine Mines. During the first half of 1980 the Contractor for the Lessees placed a mining plant, camp facilities and a 150 ton per day modular mill on site. At the same time the shaft was deepened 200 feet to 1,050 feet. Expenditures by the Lessees to June 30th for preproduction work, equipment purchases and inventory amounted to \$5,875,585.

Limited production began in July and has continued since that time. Up to the year end only 12,282 tons were milled grading 0.472 ounces gold per ton which produced 4,738 ounces gold and 1,291 ounces of silver. An operating loss of \$856,000 was incurred. Grade of ore to the mill was lower than previously estimated due principally to dilution caused by a barren dyke which unexpectedly cut through the vein below the 600 foot level, and to dilution resulting from mechanized raising. Mill recovery was much lower than the 98.5% recovery achieved by Discovery when 13,000 tons were mined and milled in 1962-3. Intermittent operating performance and mill circuit problems appear to be the principal causes. Substantial improvements to the operation have been made since year end and better results are anticipated. Ore reserves at January 1st, 1981 above the 1,000 foot level are estimated by the lessees at 30,250 tons grading 0.58 ounces gold per ton. We are advised that the current gold price of US \$500 precludes plans to deepen the

DISCOVERY MINES LIMITED

shaft below the 1,000 foot level. Indications, therefore, are that the lessees may not recover their investment.

Terms of the lease with Noranda and Pamour call for first cash flow from production to be applied to the recoupment of preproduction costs pro rata with payment to Discovery of \$600,000. After all cost recoupment, cash flow is to be divided 70% to Noranda and Pamour, 20% to Discovery and 10% to Camlaren until 50,000 tons have been milled. Thereafter profits to Discovery and Camlaren are to increase to 26.7 and 13.3 per cent, respectively. In addition to ownership of a two-thirds interest in the Gordon Lake property, Discovery also holds 65.5% of Camlaren's issued shares.

EXPLORATION AGREEMENTS

Exploration agreements have been made on three of Discovery's gold properties. At LaForma, in the Yukon Territory, the East Block claims have been optioned to Arctic Red Resources Corporation for cash payments aggregating \$100,000 and a net smelter royalty of 3%. The claims are underlain by a mineralized intrusive, and geochemical surveys indicate that there is an area 1,400 feet long by 1,600 feet wide that is anomalously high in gold and associated metals.

In a separate agreement with Arctic Red governing the LaForma mine claims, that company has committed to spend \$400,000 by October 31, 1982 on underground exploration of the G-3 Zone. There are estimated reserves of 68,500 tons with an average grade of 0.44 ounces gold per ton above the lowest adit level. Diamond drilling to a depth of 400 feet below this level has returned several ore grade intersections. Discovery will have a 5% net smelter return royalty if the property is brought into production. Until the property is in commercial production, Discovery is to receive advance royalty payments of \$25,000 in 1983, 1984 and 1985; thereafter, annual advance royalty payments are to increase at a rate of \$25,000 per year up to a maximum annual payment of \$200,000.

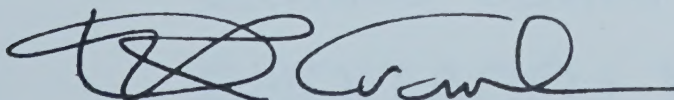
An agreement with a major corporation is in the final stages of completion regarding the original Discovery gold mine property and a large area in the vicinity of the property. The optionee plans significant exploration expenditures and can earn a 60% interest. Discovery would then have a 40% working interest or a 15% carried interest in the claim groups. Field work will commence this summer.

FINANCIAL

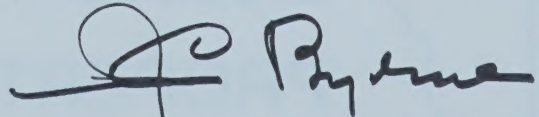
Discovery's working capital increased by \$1,806,000 during the year, from a deficit of \$994,000 at the end of 1979 to a positive figure of \$812,000 at the end of 1980. The improvement resulted from a fixed price sale of 700,000 treasury shares and proceeds received from the sale of investments.

Your company holds effective control of Rayrock Resources Limited, a company which is active in mining and oil and gas exploration and production. The market value of our Rayrock holdings at year end was \$7,244,000 compared with the book value on the balance sheet of \$1,461,000.

On behalf of the Board

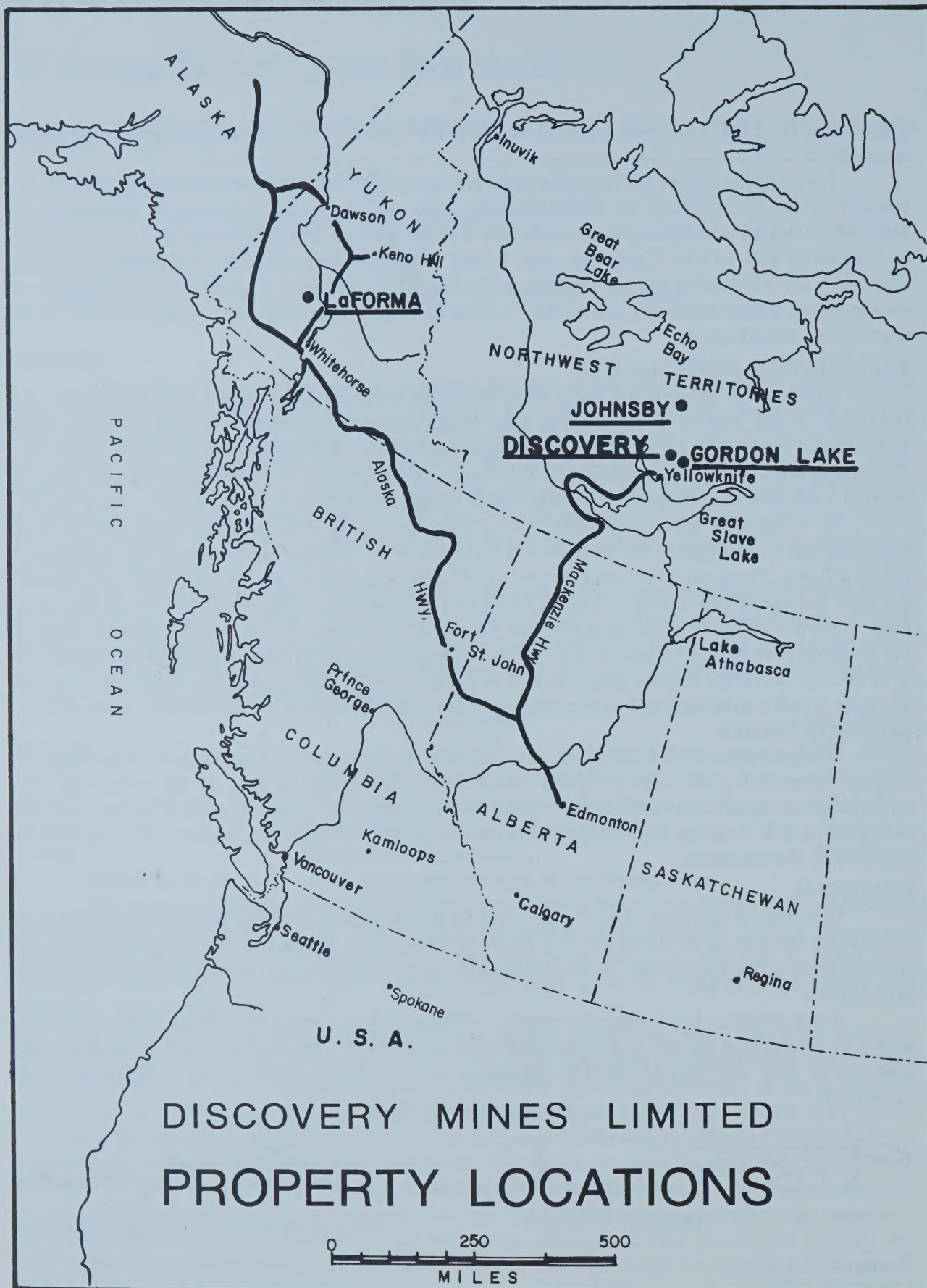


President and Operations Manager



Chairman and Chief Executive Officer

Toronto, Ontario
March 20, 1981



Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Discovery Mines Limited as at December 31, 1980 and the consolidated statements of earnings, deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1980 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Canada
March 16, 1981

COOPERS & LYBRAND
Chartered Accountants

DISCOVERY MINES LIMITED

Consolidated Balance Sheet

ASSETS		1980	1979
Current Assets			
Cash and term deposits		\$ 816,577	\$ 13,331
Accounts receivable and prepaid expenses		26,707	14,477
Income taxes recoverable		7,000	11,000
		<u>850,284</u>	<u>38,808</u>
Long-term investments (notes 1(b) and 2)		<u>1,623,080</u>	<u>2,004,005</u>
Mining properties (notes 1(c), 1(d) and 3)			
Mining claims		342,615	342,615
Furniture and equipment		475	596
Deferred exploration and development expenditures		<u>1,113,862</u>	<u>1,113,862</u>
		<u>1,456,952</u>	<u>1,457,073</u>
Petroleum and natural gas leases — at cost, less accumulated depletion of \$65,345 (1979 — \$37,116) (notes 1(c) and 1(d))		<u>356,457</u>	<u>254,883</u>
Deferred charges (note 8)		<u>70,952</u>	<u>—</u>
Goodwill (note 4(b))		<u>15,801</u>	<u>—</u>
		<u>\$4,373,526</u>	<u>\$3,754,769</u>

DISCOVERY MINES LIMITED

as at December 31, 1980

LIABILITIES

Current liabilities

	1980	1979
Bank indebtedness	\$ —	\$ 802,000
Accounts payable and accrued liabilities	38,699	15,969
Due to Rayrock Resources Limited	—	215,200
	38,699	1,033,169
Minority interest	27,244	29,868
	65,943	1,063,037

SHAREHOLDERS' EQUITY

Capital stock (note 4)

Authorized —		
2,000,000 preference shares of \$1 par value		
6,000,000 common shares of no par value		
Issued and fully paid —		
4,255,630 common shares (1979 — 3,538,773)	4,640,630	3,398,773
Contributed surplus	506,774	506,774
Deficit	(839,821)	(1,213,815)
	4,307,583	2,691,732
	<u>\$4,373,526</u>	<u>\$3,754,769</u>

Signed on behalf of the Board

J. C. BYRNE, Director
H. J. WHELAN, Director

DISCOVERY MINES LIMITED

Consolidated Statement of Deficit

For the Year Ended December 31, 1980

	1980	1979
Deficit — beginning of year		
As previously reported	\$1,213,815	\$1,249,517
Prior period adjustment of minority interests	—	(9,558)
As restated	1,213,815	1,239,959
(Earnings) for the year	(414,788)	(29,305)
Share of retained earnings adjustment of significantly influenced company	—	3,161
Share issue expenses less share of expenses determined by the equity method (\$22,405)	40,794	—
Deficit — end of year	\$ 839,821	\$1,213,815

Consolidated Statement of Earnings

For the Year Ended December 31, 1980

	1980	1979
Income		
Revenue from petroleum operations	\$ 151,545	\$ 169,571
Investment income	71,907	3,500
Gain on sale of investments	17,543	111,873
	240,995	284,944
Expenses		
Cost of petroleum production	75,190	86,537
Royalty taxes (recoverable)	(7,815)	(13,909)
Bad debts	—	32,000
Head office	154,212	53,769
Bank interest	11,185	94,790
Depreciation and depletion	28,348	27,703
General exploration	67,849	—
	328,969	280,890
(Loss) earnings before the undernoted items	(87,974)	4,054
Share of earnings determined by the equity method	109,901	25,251
	21,927	29,305
Income taxes recoverable —		
Deferred	46,327	—
Earnings before extraordinary items	68,254	29,305
Extraordinary items (note 6)	346,534	—
Earnings for the year	\$ 414,788	\$ 29,305
Earnings per share before extraordinary items (note 7)	\$0.02	\$0.01
Earnings per share for the year (note 7)	\$0.11	\$0.01

DISCOVERY MINES LIMITED

Consolidated Statement of Changes in Financial Position

For the Year Ended December 31, 1980

	1980	1979
Source of working capital		
Proceeds on issue of treasury stock	\$1,241,857	\$ —
Proceeds on sale of fixed assets	—	232
Proceeds on sale of investments	99,158	129,328
Proceeds on sale of shares of Rayrock Resources Limited	1,015,306	—
	<u>2,356,321</u>	<u>129,560</u>
Use of working capital		
(Earnings) before extraordinary items	(68,254)	(29,305)
Items not affecting working capital —		
Recovery of deferred taxes	46,327	—
Depreciation and depletion	(28,348)	(27,703)
Gain on sale of investments	17,542	111,873
Gain on sale of fixed assets	—	232
Share of earnings determined by the equity method	109,901	25,251
Other	—	(12,698)
	<u>77,168</u>	<u>67,650</u>
Advances to Avoca Mines Canada Limited	—	198
Development expenditures — deferred	—	132
Purchase of investments	192,397	819,150
Purchase of oil and gas properties	129,802	—
Deferred Charges	70,952	—
Share issue expenses	63,199	—
Acquisition of subsidiary company (note 4(b))	16,857	—
	<u>550,375</u>	<u>887,130</u>
Increase (decrease) in working capital	1,805,946	(757,570)
Working capital (deficiency) — beginning of year	(994,361)	(236,791)
Working capital (deficiency) — end of year	\$ 811,585	\$ (994,361)

DISCOVERY MINES LIMITED

Notes to Consolidated Financial Statements FOR THE YEAR ENDED DECEMBER 31, 1980

1. ACCOUNTING POLICIES

(a) Basis of consolidation

The consolidated financial statements include the accounts of the company and its subsidiary, Camlaren Mines Limited. The accounts of a subsidiary company, Avoca Mines Canada Limited, have not been consolidated herein because that company is currently being supported by the government of Ireland and increases in equity are not likely to accrue to the parent company. The investment in Avoca is carried at nominal value. Investments in significantly influenced companies are accounted for by the equity method.

(b) Long-term investments

The investment in shares of significantly influenced companies is carried at cost adjusted by the company's share of their earnings or losses since significant influence was obtained.

Other long-term investments are written down when there is evidence that their inherent worth has declined below their carried value.

(c) Deferred exploration and development expenditures

These expenditures are deferred until such time as they are written off against production from the property to which they apply or until the claims are sold or otherwise disposed of. Expenditures made in the general search for minerals are normally charged to expense in the year incurred.

Costs incurred in exploring for oil and gas, including participations in joint ventures, are capitalized until completion of the particular exploration programme, at which time the costs of dry holes are written off. Acquisition costs of oil and gas properties and the costs of drilling and equipping successful wells are capitalized.

(d) Depreciation and depletion

Depreciation on equipment is provided on a declining balance basis at a rate of 20% per annum. Depletion of oil and gas properties and drilling costs is determined partly by the unit-of-production method based on proven reserves and partly on a straight-line basis over 144 months.

2. LONG-TERM INVESTMENTS

	1980	1979
(a) Investment in companies accounted for by the equity method —		
Common shares (notes 1(b) and 2(b))	\$1,465,646	\$1,898,854
Preference shares	100,000	100,000
Debentures	4	1
	<u>1,565,650</u>	<u>1,998,855</u>
Other investments — at cost —		
Shares (notes 1(b) and 2(c))	57,430	5,150
	<u>\$1,623,080</u>	<u>\$2,004,005</u>

(b) The quoted market value of the common shares in companies accounted for by the equity method is \$7,244,000 (1979 — \$3,417,000).

(c) Other investments consist of listed shares carried at cost of \$57,430 with a quoted market value of \$53,500 (1979 — \$5,150 and \$5,500, respectively).

(d) The quoted market values referred to above do not necessarily represent the realizable value of these holdings which may be more or less than that indicated by market quotations.

DISCOVERY MINES LIMITED

3. MINING PROPERTIES

	<u>1980</u>	<u>1979</u>
(a) Mining claims acquired for cash and shares of capital stock as valued by the directors of the applicable company — at cost, less amounts written off:		
32 claims Whitehorse, Yukon Territory	\$ 69,312	\$ 69,312
27 claims Discovery, N.W.T.	1	1
21 claims Gordon Lake Area, N.W.T.	273,300	273,300
Sundry	2	2
	<u>\$342,615</u>	<u>\$342,615</u>
(b) Deferred exploration and development expenditures (note 1(c)):		
Camlaren Project	<u>\$1,113,862</u>	

The company and Camlaren Mines Limited have entered into an agreement with Noranda Mines Limited (Noranda) and Pamour Porcupine Mines Limited (Pamour) wherein Noranda and Pamour have placed the gold mining property situated on Muir Island in Gordon Lake, Northwest Territories, into production. The company has direct and indirect interests totalling approximately 89% in the mining property.

Under the agreement, cash flow from production will be applied to the recoupment by Noranda and Pamour of the capital and operating costs, pro rata with the payment to Discovery of \$600,000, representing previous expenditures by Discovery on the Gordon Lake property. After all cost recoupment, cash flow will be divided 70 percent to Noranda and Pamour, 20 percent to Discovery and 10 percent to Camlaren until 50,000 tons of ore have been milled. Thereafter profits will be divided 60 percent to Noranda and Pamour, 26.7 percent to Discovery and 13.3 percent to Camlaren.

- (c) The company is in the process of exploring and developing its mineral properties. The recoverability of the amounts shown for mineral properties and related deferred costs is dependent upon the existence of economically recoverable reserves, the ability of the company to obtain necessary financing to complete the development and upon future profitable production.

4. CAPITAL STOCK

During the year, the company issued common shares from its treasury as follows:

- (a) 700,000 shares at \$1.75 each for proceeds of \$1,225,000. The net cost of issuing these shares amounting to \$40,794 was charged to deficit.
- (b) 16,857 shares at an assigned value of \$1 each for proceeds of \$16,857 to purchase all of the remaining outstanding shares of Botha Lake Mining Corporation, which was subsequently wound-up into the company. The difference between the value of the shares issued and the underlying book value of the assets acquired was charged to goodwill. Goodwill will be amortized over 2 years commencing in 1981.
- (c) Officers and employees of the company have been granted stock options to purchase 99,000 shares of the company at a price of \$4.61 per share. These options are exercisable to December 31, 1983.

5. REMUNERATION OF DIRECTORS AND SENIOR OFFICERS

- (a) Directors and senior officers, as defined in The Business Corporations Act of Ontario, received direct remuneration in the year ended December 31, 1980 of \$6,000 (1979 — \$2,500).
- (b) Rayrock Resources Limited pays substantially all the remuneration of directors and senior officers of the company and other associated companies, and is reimbursed by these companies for their proportionate share thereof.

DISCOVERY MINES LIMITED

6. EXTRAORDINARY ITEMS

Gain on sale of 400,000 shares of Rayrock Resources Limited (net of \$130,609 deferred tax provision)	\$358,124
Realization of previously unrecorded deferred taxes as a result of sale of shares	84,282
	<u>442,406</u>
Share of extraordinary items of Rayrock Resources Limited determined by the equity method	212,742
	<u>655,148</u>
Less: Equity adjustment thereon — portion of extraordinary items applicable to Rayrock shareholders other than Discovery	(308,614)
	<u>\$346,534</u>

7. EARNINGS PER SHARE

The company's investment in Rayrock Resources Limited (20.8%) and Rayrock Resources Limited investment in the company (41.0%) mean that the company has a 8.5% pro rata interest in its outstanding shares held by Rayrock Resources Limited. Consequently, these reciprocal shareholdings have been taken into account in determining the number of Discovery Mines Limited shares outstanding for purposes of computing earnings per share. The weighted average number of shares used in the calculation is 3,712,108 (1979 — 3,041,823).

8. RELATED PARTY TRANSACTIONS

- During the year the company purchased 10,000 shares and sold 40,000 shares of Rayrock Resources Limited (Rayrock) to hold 950,000 shares at December 31, 1980. The company owns an additional 100,000 6% cumulative preferred shares of Rayrock, which in turn owns 41% of the company's outstanding shares.
- Rayrock pays substantially all of the remuneration of directors and senior officers together with the rent and other joint costs (including general exploration) of associated companies, and is reimbursed by the company for their proportionate share thereof. The amount paid during the year by the company in respect of such charges was \$63,200 (1979 — \$21,680).
- During the year the company contributed \$94,603 towards a past service pension for a senior executive. This contribution is being expensed over four years commencing in 1980.

9. INCOME TAXES

- The company has approximately \$1.6 million of deferred exploration and development expenditures available for income tax purposes which may be applied against income of future periods.
- The company has losses carried forward for income tax purposes of approximately \$258,000 which expire as follows:

1981	\$ 77,000
1982	122,000
1983	<u>59,000</u>
	<u>\$258,000</u>
- The potential tax benefits arising from the deferred exploration and development expenditures and the loss carry-forwards have not been recognized in these consolidated financial statements.

